

**VIRGINIA PORT AUTHORITY
NORFOLK, VIRGINIA**

**REPORT ON AUDIT
FOR THE YEAR ENDED
JUNE 30, 2002**



AUDIT SUMMARY

Our audit of the Virginia Port Authority for the year ended June 30, 2002, found:

- internal control matters listed below that we consider to be reportable conditions; however, we do not consider any of these to be material weaknesses;
 - Strengthen Controls Over Travel Regulations
 - Develop Procedures for Amending Contracts
- no material instances of noncompliance with laws and regulations that are required to be reported;
- adequate corrective action of prior audit findings except for the matters listed below;
 - Mitigate Possible Conflict of Interest of Capital Projects.

- TABLE OF CONTENTS -

	<u>Pages</u>
AUDIT SUMMARY	
INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING	1-2
INTERNAL CONTROL FINDINGS AND RECOMMENDATIONS	3-4
OFFICIALS PAGE	5

November 7, 2002

The Honorable Mark R. Warner
Governor of Virginia

The Honorable Kevin G. Miller
Chairman, Joint Legislative Audit
and Review Commission

Board of Commissioners
Virginia Port Authority

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND ON
INTERNAL CONTROL OVER FINANCIAL REPORTING

We have audited the financial statements of the governmental activities and each major fund of the Virginia Port Authority, a component unit of the Commonwealth of Virginia, as of and for the year ended June 30, 2002, and have issued our report thereon dated November 7, 2002. Our report on the financial statements is included in the Financial Report issued by the Port Authority. We submit herewith our report on compliance and internal control over financial reporting.

In planning and performing our audit of the financial statements of the Port Authority as of and for the year ended June 30, 2002, we considered internal controls over financial reporting and tested compliance with certain provisions of laws, regulations, contracts, and grants in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards.

Compliance

As part of obtaining reasonable assurance about whether the Port Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under Government Auditing Standards.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Port Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Port Authority's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the section entitled, "Internal Control Findings and Recommendations."

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe none of the reportable conditions described above is a material weakness.

The Port Authority has not taken adequate corrective action with respect to the previously reported finding "Provide Adequate Oversight of Capital Projects and Mitigate Possible Conflict of Interest." Accordingly, we included this issue entitled "Mitigate Possible Conflict of Interest of Capital Projects" in the section entitled "Internal Control Findings and Recommendations." The Port Authority has taken adequate corrective action with respect to audit findings reported in the prior year that are not repeated in this report.

The "Independent Auditor's Report on Compliance and on Internal Control Over Financial Reporting" is intended solely for the information and use of the Governor and General Assembly of Virginia, the Board of Commissioners and management, and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

EXIT CONFERENCE

We discussed this report with management at an exit conference held on December 19, 2002.

AUDITOR OF PUBLIC ACCOUNTS

DBC:whb
whb:52

INTERNAL CONTROL FINDINGS AND RECOMMENDATIONS

Mitigate Possible Conflict of Interest of Capital Projects

In prior fiscal years, the Port Authority awarded two sole source contracts for project management and general capital project consulting to the same engineering firm that already had several on-going capital project contracts. In addition to the aforementioned, the Port Authority issued two additional term contracts to the engineering firm in the current fiscal year. Amounts disbursed to the firm equaled \$1.7 million and \$3.4 million in 2001 and 2002, respectively. As noted in the prior year finding, we believe the project management contract may be a possible conflict of interest on the part of the vendor since the vendor could be supervising and reviewing its own work.

The Port Authority has addressed oversight and billing issues raised in the prior year. The Port Authority has requested and obtained comprehensive billings and hired a chief engineer in June 2002. However, we found where multiple vendor employees charged hours for the Norfolk International Terminal South project while at the same time charging hours as program managers for the same project. Because we were unable to determine the appropriateness of the bill, the potential conflict of interest still exists.

Since the Port Authority continues to enter into various contracts with the same engineering firm that it hired to manage the day-to-day activities of all capital outlay consultants, the potential for conflict continues to exist if the vendor employees supervise themselves. Management should continue to implement effective oversight procedures to mitigate this contractual arrangement as soon as possible and should avoid similar situations in the future.

Strengthen Controls Over Travel Regulations

As noted in prior years, the Port Authority has numerous exceptions to state travel regulations that provide agency personnel with maximum flexibility while on official business for marketing purposes that involve prospective clients. These exceptions do not alleviate the agency's responsibility for safeguarding against reimbursing unnecessary or disallowed travel expenses. In fiscal year 2002, the Port Authority had over \$650,000 in travel expenses.

As indicated by the following, the Port Authority needs to strengthen controls over travel guidelines:

- The Port Authority does not require itemized receipts for reimbursement of meals and entertainment expenses, when employees incur costs for themselves and potential clients, as mandated by the State Travel Regulations. In four of five travel vouchers tested totaling \$16,315, the supporting documentation used by the Port Authority to reimburse employees for meal and entertainment expenses was a hotel or a credit card receipt in summary format. Without a detailed receipt, it is not possible to determine whether meal and entertainment expenses are reasonable.

As set forth in the Appropriation Act, the Port Authority is "authorized to expend from special funds amounts not to exceed \$25,000 for entertainment expenses commonly borne by businesses." In addition, the Act requires a separate recording of these expenses. Examples of these expenses include alcohol served with clients, golf outings with clients, and tobacco products given for promotional gifts. The Port Authority has set up an account to record and monitor such expenses but lacks a complete inventory of detailed receipts needed to appropriately track expenses.

- In four of five instances reviewed, the Port Authority failed to perform a cost benefit analysis as mandated by the State Travel Regulations when using the state-owned airplane at a total cost of \$15,745. The cost benefit analysis should include a comparison of the total cost of the trip by both means, commercial versus private or chartered air travel. By not following state regulations and not performing the analysis, it is not possible to determine if the Port Authority used the state plane for convenience rather than for cost saving measures.
- The Port Authority reimbursed employees for meal expenses that exceeded the per diem rate. Travel regulations allow for the reimbursement of actual business meal expenses up to the applicable per diem rate. In the seven business meals reviewed, the Authority exceeded the per diem rate.
- The Port Authority did not properly monitor and record petty cash funds disbursed as “permanent travel advances.” On three occasions, employees resigned and the Port Authority failed to collect the travel advance. This resulted in the loss of \$4,318.

The Port Authority should comply with the State Travel Regulations. To achieve compliance, Port Authority personnel must submit original itemized receipts for reimbursement, perform a cost benefit analysis when using the State-Owned Airplane, reimburse employees at the appropriate per diem rate, and upon resignation withhold an employee’s final pay until the Port Authority is fully reimbursed for any outstanding travel advances. By following these regulations, the Port Authority will be able to appropriately monitor travel and entertainment expenses as well as significantly reduce the risk of inappropriate charges.

Develop Procedures for Amending Contracts

The Port Authority does not have policies and procedures to address amending contracts. In five out of nine contracts reviewed, the Port Authority amended existing contracts. These amendments increased the dollar value and in some instances, significantly altered the scope of work of the original contract. In one instance, ratified amendments increased the total value of the contract by six million dollars. The Port Authority executed the amendments without written justification or documented negotiation.

The Port Authority is exempt from the Public Procurement Act with the caveat that procedures, which ensure fairness and competitiveness of goods and services and the administration of its capital outlay program, are in place. The Port Authority should develop procedures for amending contracts and have these procedures reviewed and approved by the Bureau of Capital Outlay officials. Procedures should include required detailed justification and management approval. In addition, the Port Authority should establish a dollar or percent change threshold for amendments, over which the agency should seek competitive procurement.

Establishing appropriate policies is key for implementing a comprehensive structure to ensure fair competition of goods. The Port Authority has recognized the need to implement such procedures and has developed draft policies. Management should work towards the conversion of policies into action and have the procedures approved by appropriate personnel. In addition, the Port Authority should carefully examine its needs and evaluate the scope of work before establishing a contract to minimize the necessity of amendments.

VIRGINIA PORT AUTHORITY
Norfolk, Virginia

BOARD OF COMMISSIONERS

E. Massie Valentine, Jr., Chairman

James H. Burnley, IV, Vice Chairman

William B. Bales

William H. Dickey, Jr.

William M. Grace

M. Ray Hurst, Jr.

Frank G. Louthan, Jr.

John R. Nelson

Peter D. Pruden, III

Gustav H. Stalling, III

Robert M. Tata

J. Robert Bray, Executive Director

Oliver W. Daughdrill, Treasurer

Debra J. McNulty, Clerk to the Board

